

Pass-Through Withholding and Composite Tax



What you will learn

- Pass-through withholding and composite tax and the differences between them.
- Pass-through withholding requirements
- Who can claim pass-through withholding credits
- The ins and outs of Form PT-AGR
- Composite tax requirements

What is pass-through withholding?

Pass-through withholding (PT-WH) is a tax payment made by a pass-through entity on behalf of an owner based on the distributive share of Montana source income allocated to that owner. The owner claims the PT-WH payment as a credit against their own tax liability.

What is composite tax?

Composite tax is an election. The election is made by the owner and allows the pass-through entity to file the composite tax return on the owner's behalf. An owner included in a composite tax filing is not required to file a Montana income tax return and is excluded from the PT-WH requirements.

Pass-through Withholding VS. Composite Tax

Pass-Through Withholding:

- Paid by the pass-through entity
- Required
- Owner is required to file a tax return
- Claimed as a credit
- Disregarded Entities included

Composite Tax:

- Paid by the pass-through entity
- Tax payer election
- Satisfies the owner's filing requirement
- Cannot be claimed as a credit
- Cannot be filed by a disregarded entity

Pass-Through Withholding

Legislative Changes

- **Senate Bill 386 (L. 2015)**
 - Required pass-through withholding on owners that are also pass-through entities (a.k.a. second-tier pass-through entities) and eliminated general waiver.
 - Provided new exemptions from withholding for:
 - Owners whose distributive share of Montana source income is less than \$1,000
 - Domestic (Montana) Second-Tier Pass-through entities whose interest is held entirely, either directly or indirectly, by resident individuals
 - Publicly-traded partnerships granted a waiver according to Department rules
 - Capped penalty for late filing of information return at \$2,500

Pass-Through Withholding

When is PT-WH required?

PT-WH is required on behalf of the following owners if their distributive share of Montana source income from the pass-through entity is \$1,000 or more (MCA [15-30-3313](#)):

- Non-Resident: Individuals, Estates, and Trusts (ARM [42.9.104](#))
- Foreign C-Corporations (ARM [42.9.105](#))
- Tax-Exempt Entities whose principal place of administration is outside the state of Montana (ARM [42.9.105](#))
- 2nd tier Pass-Through Entities (S-Corporations, Partnerships, and Disregarded Entities) (ARM [42.9.106](#))

Calculating Pass-Through Withholding

PT-WH is calculated by multiplying the owner's distributive share of Montana source income by the highest marginal effective income tax rate (MCA [15-30-2103](#) and [15-31-121](#)). Payment of the PT-WH liability is due on or before the original due date of the return.

Owner Type:

- Non-resident: Individuals, Estates, and Trusts
- 2nd tier Pass-Through Entities (S-Corporations, Partnerships, and Disregarded Entities)
- Foreign C-Corporations
- Tax-Exempt Entities

PT-WH Rate:

- 6.9%
- 6.9%
- 6.75%
- 6.75%

The calculation of PT-WH is reported on the owner's Montana schedule K-1.

Who can claim PT-WH Credits?

PT-WH credits follow the distributive share of Montana source income from the pass-through entity and can only be claimed by a direct or indirect owner of the entity that is responsible for paying tax on the distributive share of income. (MCA [15-30-3313\(2\) and \(3\)](#))

Owners that can claim PT-WH as a credit against their own tax liability are:

- Individuals
- Estates or trusts that do not issue taxable distributions to their beneficiaries
- Foreign c-corporations
- Tax-exempt entities

A second-tier owner that is a pass-through entity may not claim PT-WH as a refundable credit on income the entity has distributed to its owners. However, the entity may claim PT-WH as a credit against the PT-WH and composite tax liabilities the entity has calculated on behalf of its owners. (MCA [15-30-3313\(4\)](#))

Montana Form PT-AGR

What is Montana Form PT-AGR?

Montana Form PT-AGR, also known as the Pass-Through Entity Owner Tax Agreement, is an agreement between the pass-through entity and its owner that provides the entity a waiver from the PT-WH requirements. The PT-AGR is completed and signed by the owner.

By signing and submitting the PT-AGR, the owner agrees to:

- timely file their Montana income tax returns.
- timely pay taxes due.
- be subject to the state's tax collection jurisdiction.

Montana Form PT-AGR

When does Montana Form PT-AGR become invalid?

An owner's PT-AGR is revoked and considered invalid if the owner does not file their returns nor pay their tax liabilities timely. Once revoked, the pass-through entity must include that owner in a composite tax return or remit PT-WH on that owner's behalf for all future tax years

Once a PT-AGR is revoked, the owner is ineligible to apply for a new PT-AGR.

Montana Form PT-AGR

Who is eligible to file Form PT-AGR?

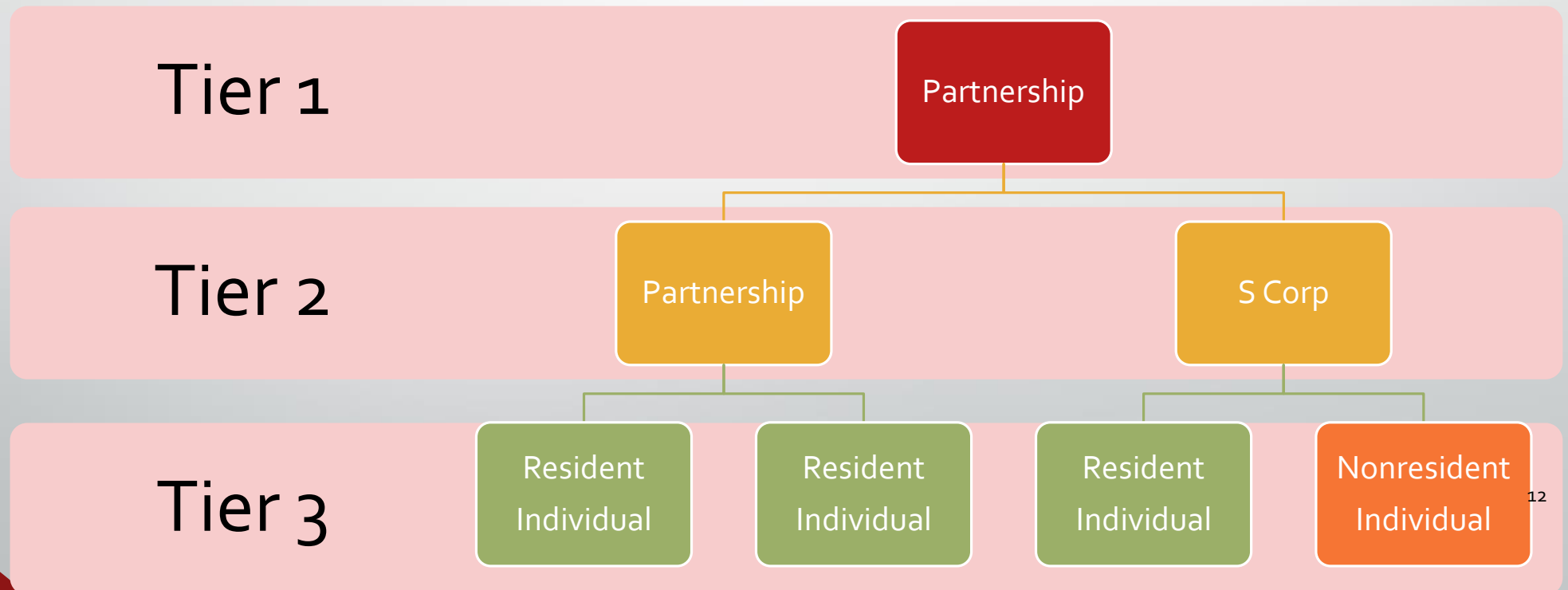
Form PT-AGR may be filed by pass-through entity owners that are:

- Nonresident individuals, estates and trusts
- Foreign C corporations (corporations not registered to do business with the Montana Secretary of State)
- Tax-exempt entities whose principal place of administration is outside the state of Montana
- Domestic second-tier pass-through entities

Montana Form PT-AGR

What is a Domestic second-tier pass-through entity?

A domestic second-tier pass-through entity is a pass-through entity whose income is ultimately distributed to and reported by resident individuals.



Completing Form PT-AGR



Pass-Through Entity Owner Tax Agreement

15-30-3313, MCA

MONTANA
PT-AGR
Rev 01 16



File online at
revenue.mt.gov

This agreement is valid for the tax year beginning and ending , and for all subsequent tax years until this agreement is revoked.

Part 1 - Pass-Through Entity Information

Entity Name		Federal Employer Identification Number	
<input type="text"/>		<input type="text"/> - <input type="text"/>	
Mailing Address			
<input type="text"/>			
City	State	Zip Code	
<input type="text"/>	<input type="text"/>	<input type="text"/>	
Pass-Through Entity Type:	<input type="checkbox"/> S corporation	<input type="checkbox"/> Partnership	<input type="checkbox"/> Disregarded Entity
Pass-Through Entity Contact Person and Phone Number			
<input type="text"/>			

Provide information about the pass-through entity in Part 1. **ALL** fields must be completed or the agreement may be rejected.

Completing Form PT-AGR

Part 2 - Owner Information			
Owner/Fiduciary Name			
Social Security Number	<input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>	OR	Federal Employer Identification Number
			<input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>
Mailing Address			
City	State	Zip Code	
Owner Entity Type:	<input type="checkbox"/> Nonresident Individual	<input type="checkbox"/> Nonresident Estate	<input type="checkbox"/> Tax-Exempt Entity
	<input type="checkbox"/> Foreign C corporation	<input type="checkbox"/> Nonresident Trust	<input type="checkbox"/> Domestic 2nd Tier Pass-Through Entity (Complete page 2.)

- Provide information about the owner in Part 2. **ALL** fields must be completed or the agreement may be rejected.
- New entity type added for domestic second-tier pass-through entities. When this box is checked, complete page 2

Completing Form PT-AGR

Part 3 - Agreement and Signature

The undersigned agrees:

- if an individual, trust or estate, to timely file a return in accordance with the provisions of 15-30-2602, MCA;
- if a C corporation, to timely file a return in accordance with the provisions of 15-31-111, MCA;
- if a domestic 2nd tier pass-through entity, to timely file a return in accordance with the provisions of 15-30-3302, MCA and establish that the entity's distributive share of Montana source income should be fully accounted for in Montana individual income tax returns;
- to timely pay all taxes imposed with respect to income of the pass-through entity; and
- to be subject to the personal jurisdiction of the state for the collection of taxes and related interest, penalties and fees imposed with respect to income of the pass-through entity.

Signature of Owner/Fiduciary

Date

Phone Number

If the owner is a foreign C corporation, print name and title of signatory.

Part 4 - Revoke the Agreement

I revoke my previously filed Form PT-AGR as an owner of the entity listed in Part 1 for the following years _____

Signature of Owner/Fiduciary

Date

Phone Number

If the owner is a foreign C corporation, print name and title of signatory.

Complete Part 3 **OR** Part 4, but not both.

- Complete Part 3 to receive a waiver from pass-through withholding.
- Complete Part 4 to revoking a previously filed PT-AGR.

Completing Form PT-AGR

Form PT-AGR, Page 2

Domestic 2nd Tier Pass-Through Entity Type

FEIN

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Domestic 2nd Tier Pass-Through Entity Owner Information (List the owners of the second-tier, third-tier, etc.)

	Name Street Address or P O Box City State Zip Code	Entity Type and Identification Number (FEIN or SSN)	FEIN of the entity that this owner has an interest and percent of the ownership
1		Entity Type <input type="text"/> <input type="text"/> <input type="text"/>	<input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>
		FEIN	<input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> %
		SSN	<input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> %
2		Entity Type <input type="text"/> <input type="text"/> <input type="text"/>	<input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>
		FEIN	<input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> %
		SSN	<input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> %
3		Entity Type <input type="text"/> <input type="text"/> <input type="text"/>	<input type="text"/> <input type="text"/> - <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>

Provide information about each direct and indirect owner of a domestic second-tier pass-through entity.

Montana Form PT-AGR

Form PR-1, Page 5 - 2016

FEIN -

Schedule III – Montana Partnership Information

Summary Schedule and Supplemental Information

Partnerships with more than 100 partners are required to e-file this form.
See instructions for more information.

Before completing columns E, F or G, read the instructions on page **XX**.

Complete columns A through D for all partners.

A	B	C	D	E	F	G
Name Street Address or PO Box City State Zip Code	Entity Type (see codes below*) and Identification Number (FEIN or SSN)	Residency Code (R/N)	MT Distributive Share	Composite Income Tax (from Schedule IV, column H)	Pass-Through Withholding (see instructions)	PT-AGR (year)
1.	Entity Type <input type="text"/>	<input type="checkbox"/> R		<input type="checkbox"/>		
	FEIN <input type="text"/>	<input type="checkbox"/> N	00	00	00	
	SSN <input type="text"/>					
2.	Entity Type <input type="text"/>	<input type="checkbox"/> R		<input type="checkbox"/>		
	FEIN <input type="text"/>	<input type="checkbox"/> N	00	00	00	
	SSN <input type="text"/>					

If an owner has filed a valid PT-AGR, report the year the PT-AGR was filed on Schedule III, Column G.


Montana Form PT-AGR

What happens if I do not withhold and do not have a valid Form PT-AGR?

The department will assess pass-through entity for withholding on behalf each nonresident owner that does not have a valid PT-AGR.

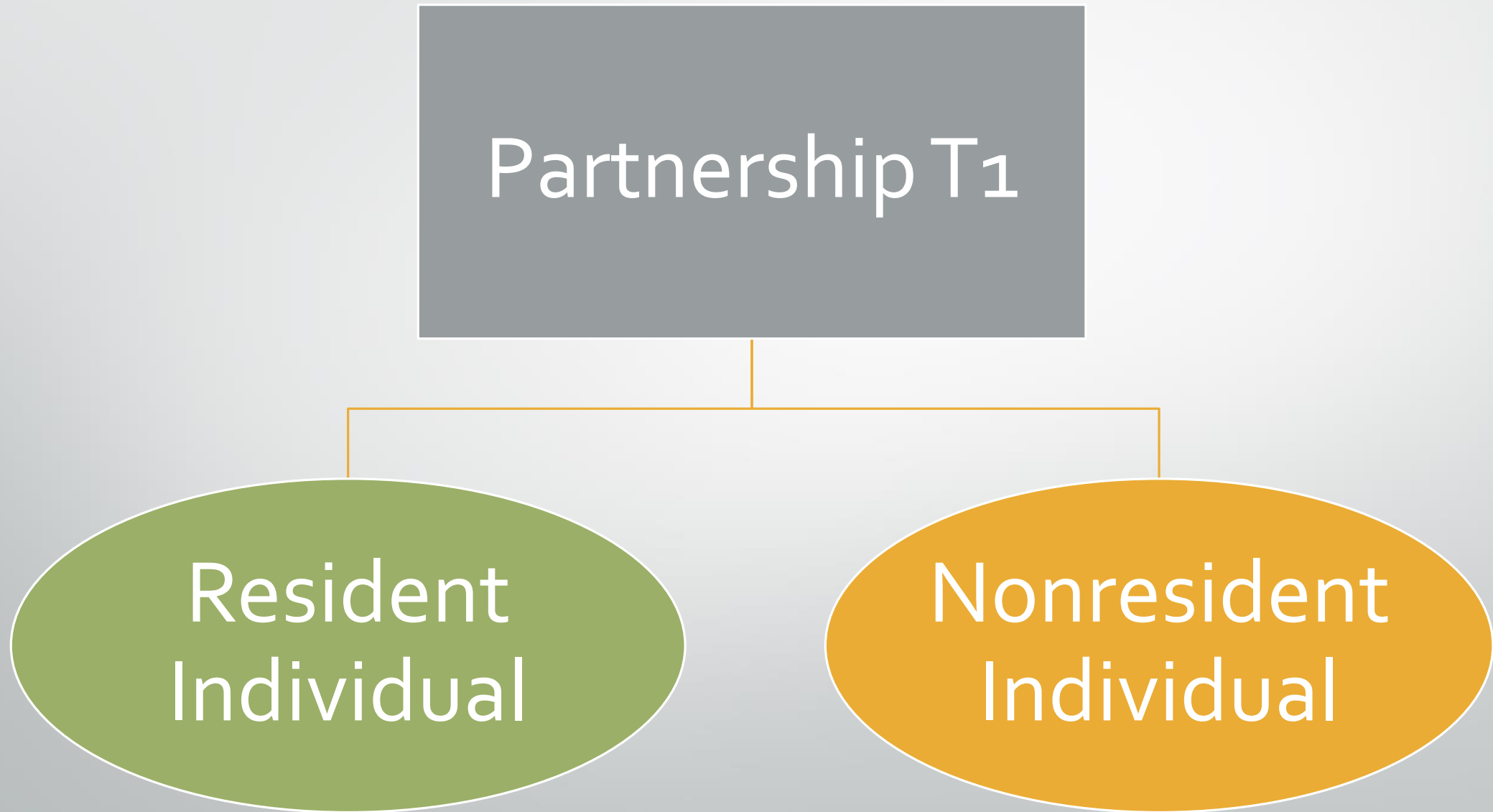
What if the owner has filed and paid tax?

The department will not assess tax, but the entity may still be liable for penalties and interest on the amount they were required to withhold.

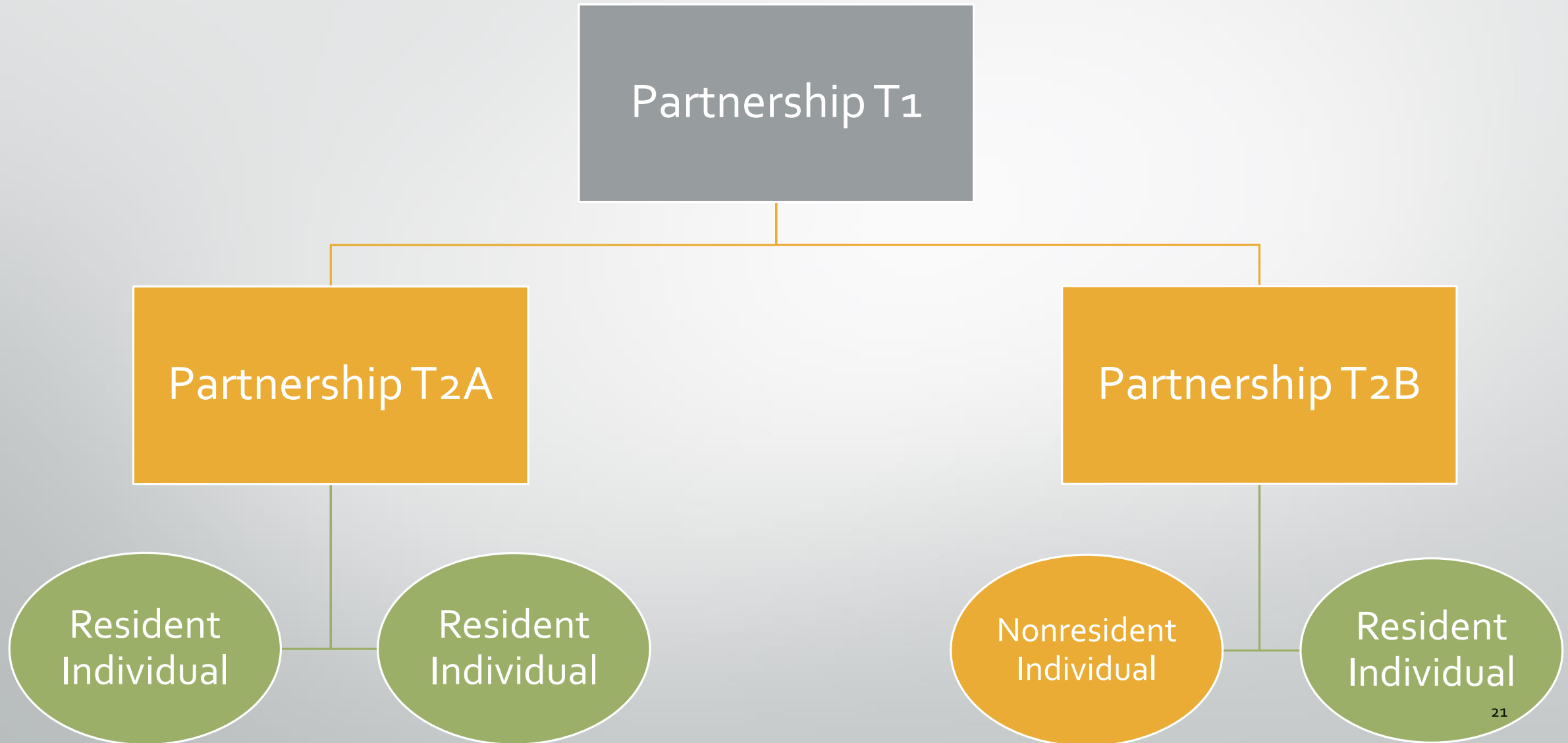


Pass-Through Withholding Examples

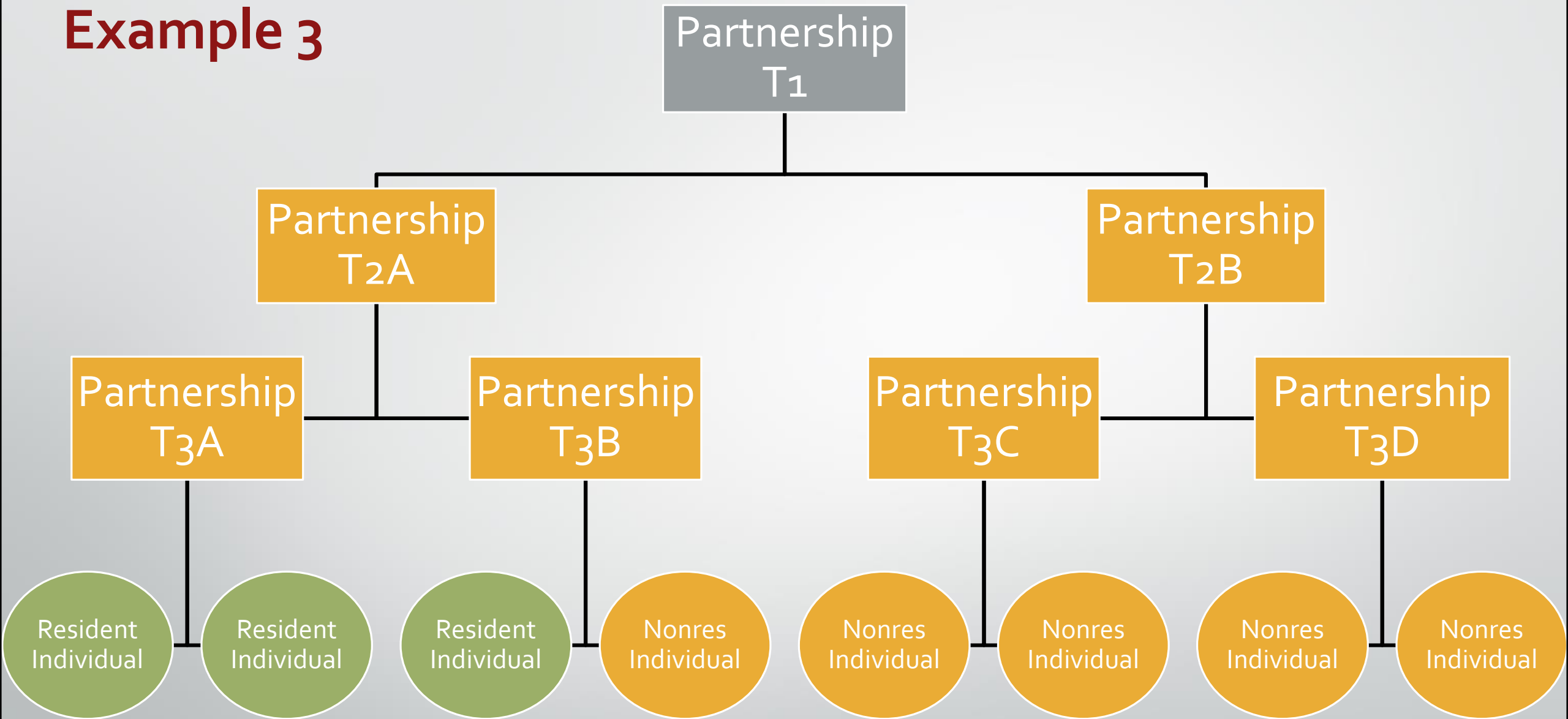
Example 1



Example 2



Example 3





Composite Tax

Composite Tax

Which owner types may be included in a composite tax election?

Only a Partnership or S-Corporation may file a composite tax return. The following owner types can be included in a composite tax return (MCA [15-30-3312](#), ARM [42.9.201](#)):

- Non-Resident: Individuals, Estates, and Trusts
- 2nd tier pass-through entities
- Foreign C-Corporations
- Tax Exempt Entities

Composite Tax

Are there other requirements to make the composite tax election?

Owners electing to be included in a composite tax return must qualify for the election. To qualify for the election an owner must:

- Have no other Montana source income
 - ✓ Montana source income from one or more pass-through entities where the owner has also made the composite tax election is okay.
- Provide written authorization (POA) to the pass-through entity to include the owner in a composite tax return.

Calculating Composite tax

The composite tax liability is calculated on Schedule IV of the pass-through entity's Montana Form PR-1 or CLT-4S.

Form CLT-4S, Page 6 - 2016

FEIN

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Schedule IV – Montana S Corporation Composite Income Tax Schedule

Part I. Eligible Participating Shareholders

Enter the number of eligible participating shareholders.

→

See instructions for more information about eligible participating shareholders.

Part II. Composite Tax Ratio

Use the amount in column 3 to complete the calculation in column H below.

1

Enter the amount from page 1, line 14 of this form.

2

Enter the amount from page 1, line 20 of this form.

3

Divide column 2 by column 1. Do not enter more than 1.000000.

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Part III. Enter below in columns A through H the required information and amounts for each eligible participating shareholder.

A	B	C	D	E	F	G	H
Name	Social security number or federal employer identification number	Shareholders' share of federal income from entity	Standard deduction	Exemption \$2,380	Montana taxable income – Subtract columns D and E from column C.	Enter the appropriate tax from the tax table below.	Montana composite income tax. Multiply column G times composite tax ratio from Part II.
1.		<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00
2.		<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00
3.		<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00	<input type="text"/> 00

Calculating Composite tax

The composite tax calculation is based on:

- The owner's share of federal income
- Less: the Montana standard deduction for a single person and one exemption
- Multiplied by the effective income tax rate and apportionment factor. (ARM [42.9.203](#))

Calculating Composite tax

Determining the owner's share of federal income.

For the purpose of calculating composite income tax:

- Divide the owner's Montana distributive share as reported on Schedule III, column D by Form PR-1, line 21 or CLT-4S, line 20 to determine ownership percentage for Montana purposes.
- Multiply the percentage by Form PR-1, line 15 or CLT-4S, line 14 to calculate the owner's share of federal income.

Calculating Composite tax

Example

Partner's Montana distributive share (Schedule III, Column D)	\$7,200
Total Montana source income (Form PR-1, Line 21)	\$12,000
Result of Schedule III, Column C divided by Form PR-1, Line 21	60.00%
Total Federal income (Form PR-1, Line 15)	\$100,000
Partner's Share of Federal Income (for composite tax purposes)	\$60,000

Calculating Composite tax

If filing a composite tax return, the pass-through entity is responsible for making quarterly estimated payments that apply toward the composite tax liability. (MCA [15-30-2512](#))



Questions?

Need Help?

Website: <http://revenue.mt.gov/>

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